Contribution of S ESOPs to participants' retirement security and employee-owner benefits

Prepared for the Employee-owned S Corporations of America

April 2022

Building a better working world

(Page intentionally left blank)

Executive summary

Since 1998, S corporations have been permitted to maintain employee stock ownership plans, a type of defined contribution retirement plan. These plans, known as “S ESOPs,” allow S corporations to provide compensation to employees and enhance their retirement security in the form of an ownership interest in the company, much like similar ESOP plans offered by C corporations.

This report analyzes trends in S ESOP retirement plans from 2002 through 2019. In particular, the analysis examines S ESOP plans’ net asset value, number of participants, average account balances, and distributions to participants. It additionally estimates the benefits to employee-owners working for S ESOP firms. The analysis relies on official filings made by companies offering S ESOPs that are publicly available from the US Department of Labor. The report does not analyze any data from 2020 or the effects of the coronavirus pandemic.

The analysis finds that both the number of people participating in S ESOP plans and the value of those plans’ net assets have increased substantially since 2002. Participants’ average account balances and the distributions paid to participants have also increased substantially. In addition, S ESOP distributions per participant were larger than distributions per participant from 401(k) plans. S ESOP employee owners likely receive thousands in direct benefits from their role as employee-owners in these companies.

Key findings include:

- **The total cumulative return per participant on average for S ESOPs from 2002 through 2019 was over $300,000 (Figure ES – 1) for a compound annual growth rate of 12.1% or approximately a third higher than returns from the S&P 500 over this time period.** Over the same time period the S&P 500 Total Returns index grew at a compound annual rate of approximately 9%. This measure of S ESOP returns includes cumulative distributions and the growth in the value of net assets, net of cumulative contributions.

- **The role of S ESOPs in enhancing retirement security grew.** Both net assets and the number of employee-owners rose significantly between 2002 and 2019. Net assets were 678% higher in 2019 ($94 billion) than in 2002 ($12 billion) and the number of participants increased by 286%, from 244,000 in 2002 to 941,000 through 2019.

- **The average S ESOP account balances was over $100,000 in 2019.** The average increased 100% from 2002, and the average S ESOP account balances was higher than any previous point in the last 15 years.

- **S ESOPs were particularly prevalent in manufacturing, professional, scientific and technical services, and construction.** Manufacturing accounted for 26% of net assets in 2019 and 30% of distributions from 2002-2019. Professional, scientific, and technical services accounted for 25% of net assets in 2019 and 21% of distributions from 2002-

2019. Construction accounted for 15% of net assets in 2019 and 12% of the cumulative distributions from 2002-2019.

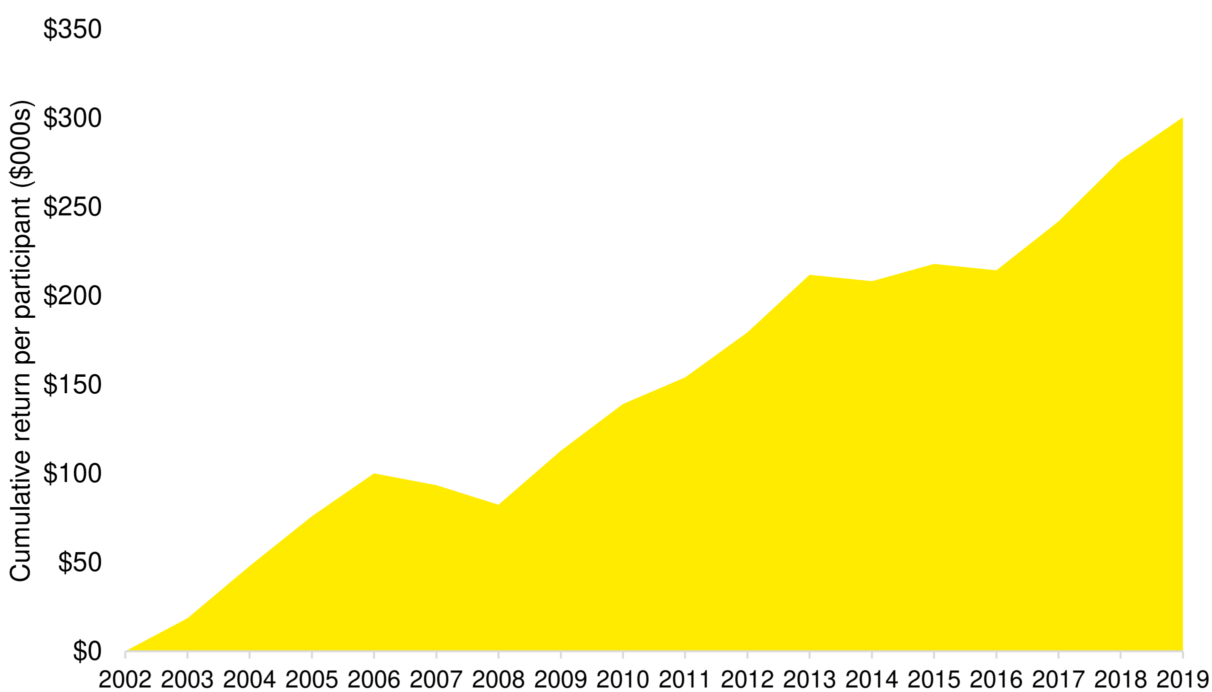
- **Distributions to participants totaled over $77 billion from 2002 through 2019, and annual distributions increased almost thirteen-fold during this period.** S ESOPs contributed to the retirement security of their participants and their contributions continued to grow with 2019 levels at an all-time high.

- **S ESOPs provided higher distributions per participant than 401(k) plans.** Post-Great Recession, the average S ESOP distribution was $1,350, or 24%, more than the average 401(k) distribution.

- **S ESOP companies were more likely to offer two retirement plans than all private sector companies were to offer a single retirement plan in 2018 (latest available).** 100% of S ESOPS offered at least one retirement plan and 57% of S ESOP companies offered an additional retirement plan, such as an additional defined benefit and/or defined contribution plan, while only 51% of all private establishments offered any retirement plan.

- **Employee-owners received an estimated annual benefit of more than $25,900 from working for an S ESOP company in 2019.** Approximately 30% of those benefits came directly from working for S ESOPs in the form of firm contributions to employee-owners' S ESOP account balances and increased job security. The remaining share was from returns in employee-owners' S ESOP account balances.

Figure ES – 1. Per participant on average total returns for S ESOPs from 2002 through 2019.



Source: US Department of Labor, Form 5500 data; EY analysis.

Contents

Contribution of S ESOPs to participants' retirement security and employee-owner benefits

I. Introduction

The Employee-owned S Corporations of America (ESCA) commissioned EY to analyze trends in the employee stock ownership plans of S corporations, known as "S ESOPs," from 2002 through 2019 and to estimate the broad benefits that S ESOPs convey to employee-owners. The analysis relies on official filings made by companies offering S ESOPs available from the US Department of Labor (DOL) and other publicly available data and research.

S corporations are domestic corporations that meet certain conditions that generally constrain their ability to raise capital through expansion of ownership and stock issuances. S corporations, for example, are limited to no more than 100 shareholders and one class of stock and are required to be a domestic corporation. Also, partnerships and C corporations cannot generally be S corporation shareholders.

Since 1998, S corporations have been permitted to maintain employee stock ownership plans, a type of defined contribution retirement plan previously only available to C corporations. These plans, known as "S ESOPs," allow S corporations to provide compensation and enhance the retirement security of employees in the form of an ownership interest in the company, similar to ESOP plans offered by C corporations.

This report analyzes trends in S ESOPs from 2002 through 2019, focusing specifically on plan net assets, participants, average account balances, distributions to participants, total return to participants, and annual benefits to S ESOP employee-owners. Duplicates were removed and updated filings were moved to the appropriate plan year. The report does not analyze any data from 2020 or the effects of the coronavirus pandemic.

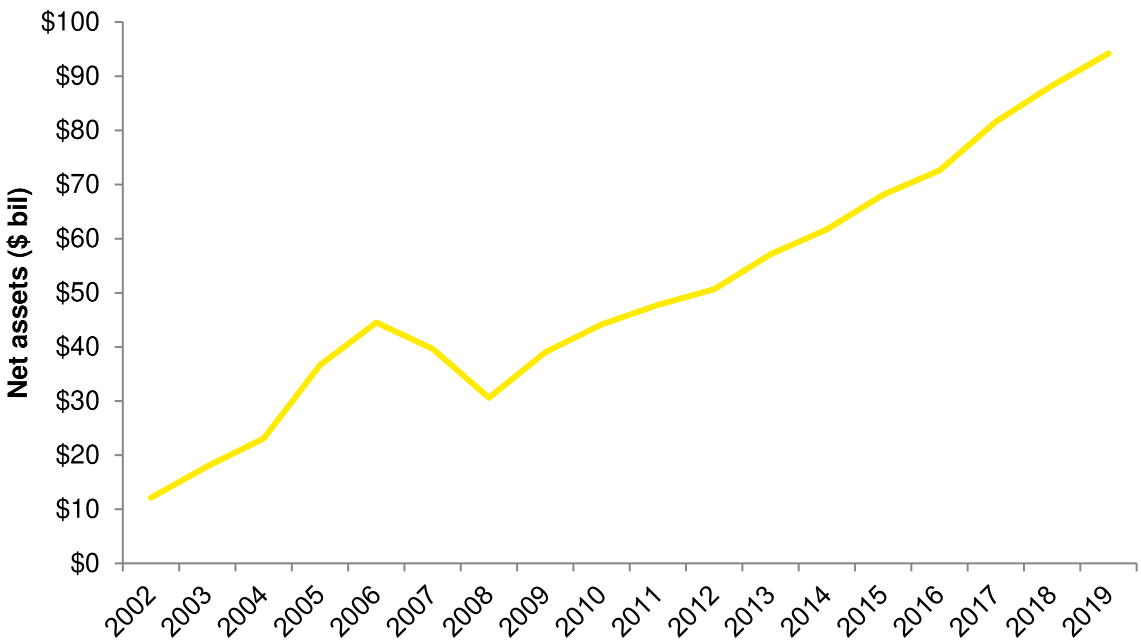
II. S ESOP account balances

A. Net assets

S corporations offering an ESOP report end of year net assets on their Form 5500. Examining these filings, this analysis finds that net assets increased 677% from $12 billion in 2002 to $94 billion through 2019 and 208% from $31 billion in 2008 to $94 billion through 2019. The compounded annual growth rate was 12.8% from 2002 through 2019. With the exception of the Great Recession, net assets in S ESOP plans consistently increased over time and peaked in 2019. This trend is displayed in Figure 1.

Figure 1. Total S ESOP net assets, 2002-2019

Billions of nominal dollars



Note: Net assets are for plans with 2019 start dates.
Source: US Department of Labor, Form 5500 data; EY analysis.

Manufacturing; professional, scientific, and technical services; and construction; account for the largest shares with wholesale and retail trade rounding out the top five industries with the highest S ESOP net assets in 2019. The top five remained similar to the results in from the previous report indicating consistent growth across industries.[1] Table 1 shows the complete industry net asset decomposition.

Table 1. Total S ESOP net assets, 2019
Billions of nominal dollars

Industry	Net assets
Manufacturing	$24.9
Professional, scientific, and technical services	23.4
Construction	14.6
Wholesale trade	8.6
Retail trade	7.8
Finance and insurance	5.1
Management of companies and enterprises	1.9
Administrative, support, and waste management	1.9
Real estate and rental and leasing	1.0
Transportation and warehousing	1.0
Health care and social assistance	0.9
Other services (except public administration)	0.7
Information	0.7
Agriculture, forestry, fishing, and hunting	0.6
Educational services	0.4
Mining	0.3
Arts, entertainment, and recreation	0.1
Utilities	0.1
Accommodation and food services	0.1

Note: Net assets by industry are for plans with 2019 start dates.
Source: US Department of Labor, Form 5500 data; EY analysis.

Professional, scientific, and technical services (NAICS 2-digit code 54) comprise a large portion of S ESOP net assets. This is a very broad industry category, encompassing everything from management consulting to translation services. However, a majority of the S ESOP assets (77%) in the professional, scientific, and technical services industry are in the architectural, engineering and related services. Architectural and engineering services accounted for 18% of all S ESOP net assets in 2019. Table 2 details the breakdown of S ESOP assets within the professional, scientific, and technical services industry.

Table 2. Net assets for professional, scientific, and technical services, 2019
Billions of nominal dollars

Industry	Net assets	Net assets share
Architectural, engineering, and related services	$17.3	74%
Consulting, research, design, and computer services	$3.0	13%
Advertising and public relations	$0.7	3%
Legal and accounting	$0.2	1%
Other	$2.2	9%
Total	$17.3	74%

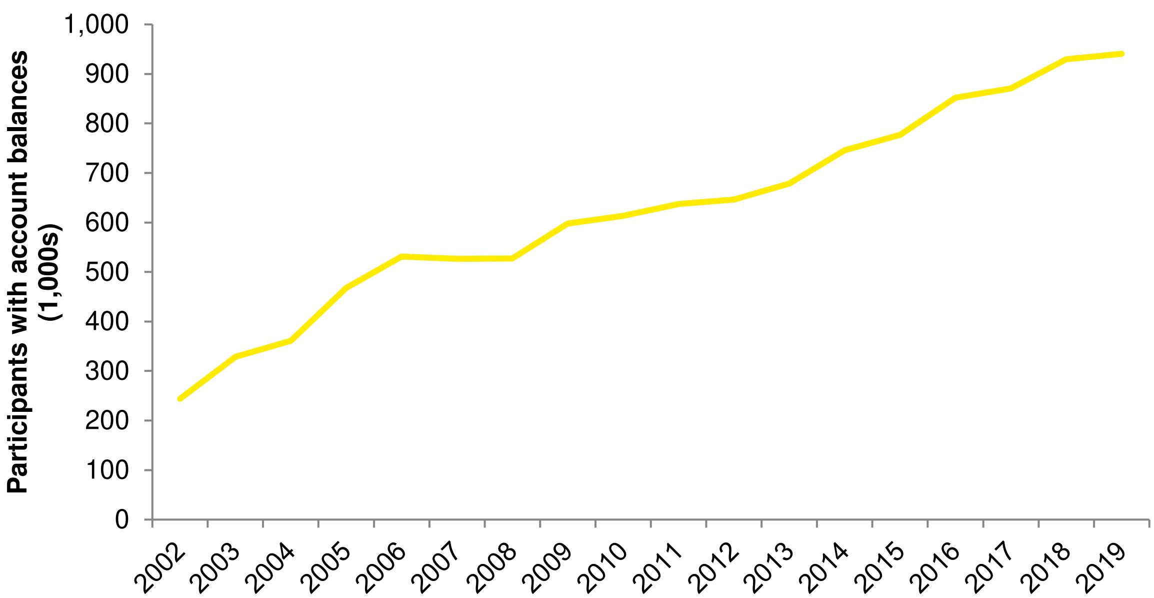
Note: Net assets by industry are for plans with 2019 start dates. "Other" includes marketing research, public opinion polling, photographic services, translation and interpretation services, veterinary services, and all other professional, scientific, and technical services. Investment firms are not included in this industry.
Source: US Department of Labor, Form 5500 data; EY analysis.

B. Participants

S ESOP plans report the number of participants with account balances, which includes all participants who have made or received a contribution in the current year or any prior year. In addition to active participants with account balances, this can include retired participants, separated participants, and deceased participants whose beneficiaries are receiving or entitled to receive future benefits.

As displayed in Figure 2, the number of S ESOP participants increased by 286% from 244,000 in 2002 to 941,000 through 2019. Part of this rise was due to a 62% increase in the number of S corporations offering ESOPs. Over time, existing S ESOPs that continue to offer the plan to new employees will often have a higher number of participants with an account balance as employees retire or leave and are replaced by new employees who participate in the plan. During the Great Recession, the number of participants with account balances fell slightly. Since the Great Recession, the number of participants with account balances has increased 57%, or by approximately 34,300 new participants per year on average and reached a historic high in 2019.

Figure 2. S ESOP participants, 2002-2019



Note: Includes all participants with account balances. For companies offering multiple ESOPs, the plan with the maximum number of participants is assumed to include all unique participants across plans.
Source: US Department of Labor, Form 5500 data; EY analysis.

Taken together, the data on net assets and number of participants suggests that the significance of S ESOPs as a retirement option continues to grow and attract businesses who want to offer their employees this benefit. In both net assets and number of participants, growth slowed due to the Great Recession, but has since rebounded.

C. Average account balances

Average account balances in 2019 were calculated using the data from the Form 5500 on end of year net assets and the estimate of participants with account balances (as displayed in Figure 2). This measure estimates the net assets held by the average participant across all S ESOP plans. While end of year net assets does not necessarily equal the sum of assets allocated to individual participants, net assets provide the best available estimate.[2]

The primary difference between net assets and account balances is in the case of leveraged S ESOPs. A leveraged S ESOP uses loans to purchase company shares, which are not immediately allocated to participants. Instead, they are held by the ESOP trust and allocated to participants' ESOP accounts as the loan is repaid. When the value of newly acquired assets equal the liability incurred to acquire them, there is no difference between net assets and assets allocated to participants. Differences can arise as the values of unallocated shares change prior to loan repayment. This report assumes that, in aggregate, plan liabilities offset unallocated plan assets.

Table 3 below displays net assets, participants with account balances, and average account balances by firm size as measured by number of employees. Also displayed is the percent of all private sector establishments with the same number of employees offering any retirement plan in 2019.[3] This indicates the prevalence of S ESOPs at various firm sizes (as measured by the number of employees). In 2019, 37% of participants with account balances (352,000) are estimated to work at firms with fewer than 500 employees. The average account balance in 2019 was $100,000, a 100% increase from 2002 and higher than any point in the past 15 years.

Table 3 also includes data from the US Bureau of Labor Statistics March 2019 National Compensation Survey that shows that employees at similarly sized establishments are less likely to have access to employer-based retirement plans.[4] Overall, just over half of all private sector establishments offered any retirement plan while 100% of S ESOP companies, by definition, offer at least one retirement plan (the S ESOP). S ESOP companies differentiate themselves from other businesses not just by offering employee ownership, but also by providing greater access to employer-based retirement plans.

Table 3. Estimated S ESOP account balances by number of employees, 2019

	S ESOPs			
Number of employees	**Net assets (billions)**	**Participants with account balances**	**Average account balances**	**% of all private establishments offering a retirement plan**
Less than 50	$3.2	41	$78,000	48%
50 to 99	$5.4	59	$92,000	77%
100 to 499	$22.3	252	$88,000	87%
More than 500	$63.2	591	$107,000	95%
	$94.2	**943**	**$100,000**	**51%**

Note: Estimated account balances are calculated by dividing net plan assets by participants with account balances. Brill (2012) reports a correlation coefficient of 0.9 between employment and active participants and that the number of employees is, on average, 40% higher than the number of active participants.[5] Therefore, estimated employment was calculated by increasing reported active participants by 40%.
Source: US Department of Labor, Form 5500 data; Bureau of Labor Statistics, National Compensation Survey (2019); EY analysis.

III. S ESOP account distributions

Distributions provide important insight into the impact of S ESOPs as they capture the income actually received by plan participants. Over time the value of an account may vary. However, for participants receiving distributions, it is the amount of the distribution that represents the benefit they ultimately receive from an S ESOP. Some S ESOP distributions are rolled over into another retirement plan where they will be invested and serve as the foundation for additional retirement security. Other S ESOP distributions will be used to pay for living expenses or moved to non-tax-preferred accounts.

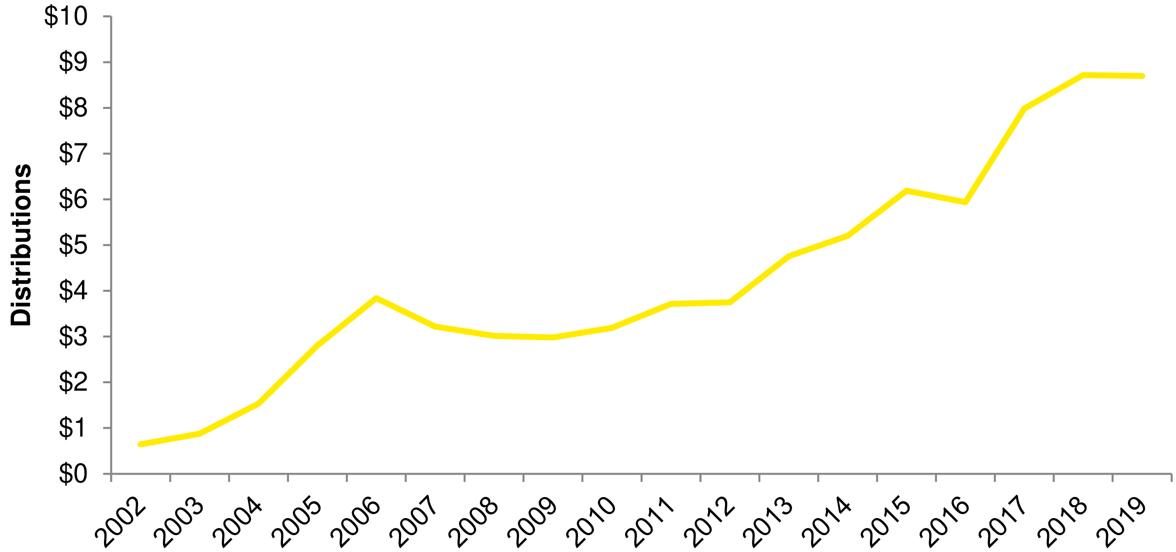
A. Data for large and small plans

Financial data for large plans with 100 or more participants is reported separately from data for small plans. Large plans are required to separately report benefits paid directly to participants or beneficiaries (including direct rollovers), payments to insurance carriers, and other payments to providers of welfare benefits. Small plans simply report total benefits paid (including direct rollovers). For each year included in the analysis, S ESOP payments to insurance carriers and other payments to providers of welfare benefits were 0.5% or less of benefits paid directly to participants or beneficiaries by large plans. This analysis assumes that payments by small plans to non-participants or non-beneficiaries were similarly immaterial.

B. S ESOP distributions

From 2002 through 2019, S ESOP distributions totaled nearly $77 billion. Since 2002, annual distributions have increased 1,249% from $645 million to more than $8.7 billion in 2019. Distributions experienced a peak in 2006 before the Great Recession at $3.8 billion and remained between $3 and $4 billion until 2012. In 2013, distributions began to grow again and increased every year except for 2016. Distributions reached a new high in 2018 of $8.7 billion and essentially remained the same in 2019. As displayed in Figure 3, the trend in S ESOPs distributions indicate a growing role for S ESOPs towards providing retirement security to employee-owners.

Figure 3. S ESOP distributions, 2002-2019
Billions of nominal dollars



Source: US Department of Labor, Form 5500 data; EY analysis.

Table 4 details S ESOP distributions by 2-digit NAICS code from 2002 through 2019. Manufacturing and professional, scientific, and technical services accounted for more than half of total distributions during this time period. The top five industries also included retail trade, construction, and wholesale trade. The data on distributions show that participants from a broad range of industries received retirement income in the form of S ESOP distributions from 2002 through 2019.

Table 4. S ESOP distributions by 2-digit NAICS code, 2002-2019
Billions of nominal dollars

Industry	**Distributions**
Manufacturing	$23.2
Professional, scientific, and technical services	16.4
Construction	9.4
Wholesale trade	8.2
Retail trade	7.6
Finance and insurance	4.0
Management of companies and enterprises	1.9
Real estate and rental and leasing	1.0
Health care and social assistance	0.9
Administrative, support, and waste management	0.9
Other services (except public administration)	0.8
Transportation and warehousing	0.7
Information	0.5
Agriculture, forestry, fishing, and hunting	0.4
Accommodation and food services	0.3
Mining	0.3
Educational services	0.2
Arts, entertainment, and recreation	0.2
Utilities	0.1
Not classified*	0.0

*Not classified indicates records that included a non-NAICS code or left the item blank.
Source: US Department of Labor, Form 5500 data; EY analysis.

As with net assets, professional, scientific, and technical services (NAICS 2-digit code 54) comprise a large portion of S ESOP distributions. Table 5 shows that the vast majority of 2019 distributions within NAICS code 54 went to participants in architectural and engineering services firms.

Table 5. Detailed distributions for professional, scientific, and technical services, 2019
Billions of nominal dollars

Industry	Distributions	Share of total
Architectural, engineering, and related services	$1.1	46%
Consulting, research, design, and computer services	$0.3	11%
Advertising and public relations	$0.0	1%
Legal and accounting	$0.0	1%
Other	$1.0	40%
Total	$2.4	100%

Note: "Other" includes marketing research, public opinion polling, photographic services, translation and interpretation services, veterinary services, and all other professional, scientific, and technical services. Investment firms are not included in this industry.
Source: US Department of Labor, Form 5500 data; EY analysis.

C. Comparisons to 401(k) distributions

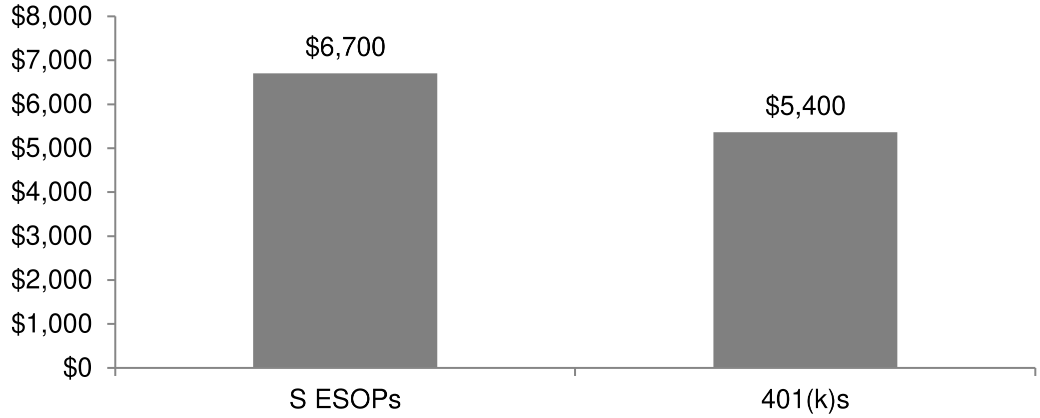
Data comparability

Distributions from S ESOP plans were compared with data on distributions from 401(k) plans as reported in the Department of Labor's Private Pension Plan Bulletin Historical Tables and Graphs.[6] The Private Pension Plan Bulletin Abstracts do not include information on S ESOPs specifically, only ESOPs generally. Form 5500 data are generally organized according to plan-year start date while the Private Pension Plan Bulletins summarize these data based on plan-year end date. To ensure that this analysis was not materially impacted by this timing discrepancy, year-lag comparisons were also used and are reported. Other minor potential discrepancies include the definition of distributions and participants. A detailed discussion of the methodology for the comparisons with the Private Pension Plan Bulletins' 401(k) data is included in the Appendix.

Distributions per participant

S ESOPs distribute 25% more on a per participant basis than 401(k) plans on average. From 2002 through 2019, S ESOP participants received an annual average of $5,900, while 401(k) plans distributed an annual average of $4,700. Focusing on average distributions after the Great Recession, as displayed in Figure 4, S ESOP participants received an annual average of $6,700, while 401(k) plans distributed an annual average of $5,400. S ESOPs distributed approximately $1,350 more (or 24%) to participants during this period. It should be noted that annual distributions can vary considerably year to year. For purposes of comparison with 401(k), active participants, which may include participants who have not yet made or received a contribution, were used.

Figure 4. Average S ESOP and 401(k) distributions per participant, 2009-2019



Note: Participants include active and retired or separated participants but excludes deceased participants whose beneficiaries are receiving or are entitled to receive future benefits. Plans using Form 5500 Short Form may include deceased participants. Distributions per participant were calculated from the average distributions for each year. Total participants include potential double-counting for employers with multiple retirement plans. Records in Form 5500 datasets are generally assigned to a year using plan-year start date, while the Private Pension Plan Bulletin uses plan-year end date.
Source: US Department of Labor, Form 5500 data; EY analysis.

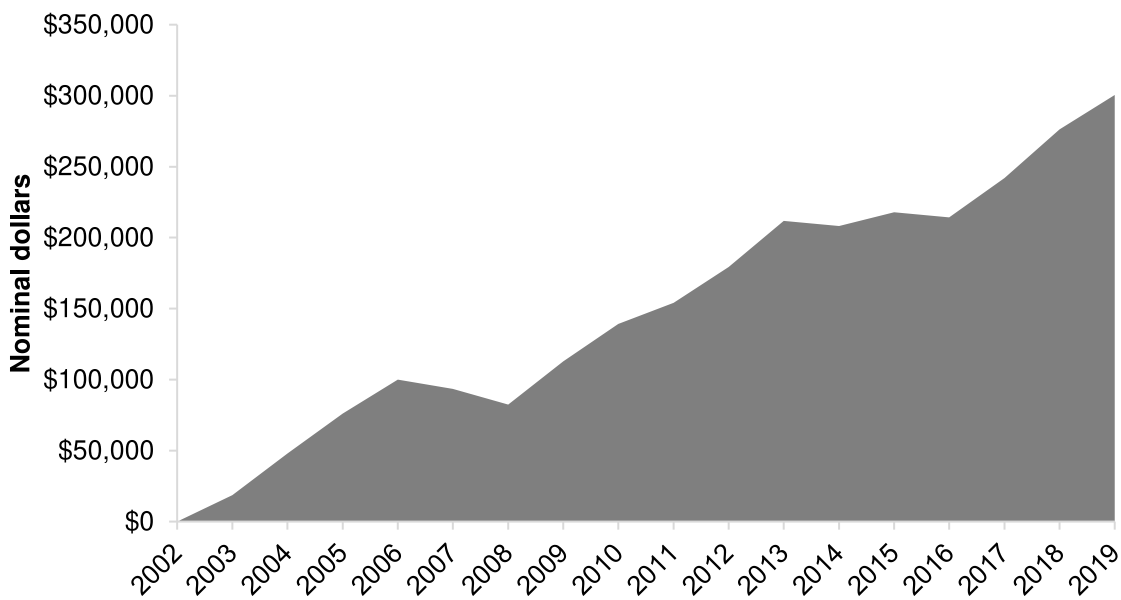
IV. Total return to participants and S ESOPs as a part of overall retirement package

A. Total return to participants

Data from all the S ESOPs that filed a Form 5500 each year from 2002 through 2019 were used to estimate the total return to S ESOP plan participants. The gain in net assets from 2002 through 2019 plus the cumulative distributions from 2003 through 2019 less cumulative contributions from 2003 through 2019 are used to estimate the total participate return. Distributions and contributions from the year 2002 were not included because 2002 net assets are calculated after the year's distributions and contributions have been made. To control for the potential increase in S ESOP net assets that occurs through an expansion of participants rather than an increase in the value of the assets held in each participant's account, the total return was estimated on a per participant basis.

From 2002 through 2019, the total return was approximately $300,000 per participant on average, for a 12.1% compound annual growth rate. Since S ESOP distributions are analogous to dividends paid to the holders of corporate stock, this return was compared to the S&P 500 Total Return Index, which includes the value of company stock plus reinvested dividends. The S&P 500 Total Return Index had a compound annual growth rate of 10.2% from 2002 through 2019. The Russell 2000 Total Returns Index grew at a compound annual rate of 7.6%. Note that the S ESOP analysis does not assume reinvestment of distributions and only considers their value at the time of distribution. These calculations and comparisons suggest that participants in S ESOPs received returns approximately a third higher than the overall stock market over this period. The return to participants on average is shown in Figure 5.

Figure 5. Per participant total returns for S ESOPs filing in 2002 and 2019



Source: US Department of Labor, Form 5500 data; EY analysis.

B. S ESOP as part of the overall private sector retirement package

For S corporations that offer an ESOP, it is typically the primary retirement plan offered. However, many companies that offer S ESOPs also offer other plans. Using reported employer identification numbers from S ESOP filings, other retirement plans offered by S ESOP companies were identified. When these additional plans are considered, S ESOP companies provided a total of \$122.6 billion in retirement assets and over \$12.1 billion in distributions in 2018.[7] These assets and distributions came from S ESOPs, other defined contribution plans, and defined benefit plans. Table 6 details the 2018 assets, distributions, and participants by type of retirement plan for all plans offered by companies with an S ESOP.

Table 6. Net assets, distributions, and participants by type of plan in S ESOP companies, 2018

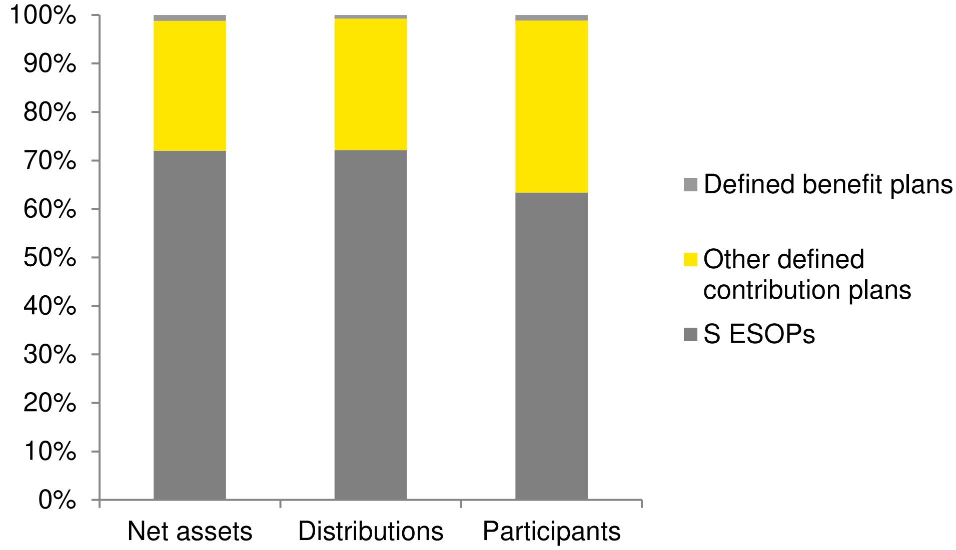
Dollars in billions, participants in thousands

	S ESOPs	Other defined contribution plans	Defined benefit plans
Net assets	\$88.3	\$32.9	\$1.4
Distributions	\$8.7	\$3.3	\$0.1
Participants	930	520	17

Note: Participants may or may not be the same individuals across plans. Participant figures for S ESOPs and other defined contribution plans include participants with account balances while the participant figure for defined benefit plans includes active participants, retired and separated participants receiving or entitled to receive future benefits, and beneficiaries of deceased participants receiving or entitled to receive future benefits.
Source: US Department of Labor, Form 5500 data; EY analysis.

By definition, 100% of S ESOP companies offer a retirement plan, but 58% offer at least one other plan. Comparatively, only 51% of all private sector establishments offer any retirement plan. In other words, S ESOP companies are more likely to offer two plans as compared to private sector establishments. A potentially important caveat to this finding is that the participants across various employer plans could be different individuals. Figure 6 shows the shares of total net assets, distributions, and participants in 2018 by plan type for companies offering an S ESOP.

Figure 6. Shares of net assets, distributions, and participants at S ESOP companies by plan type, 2018



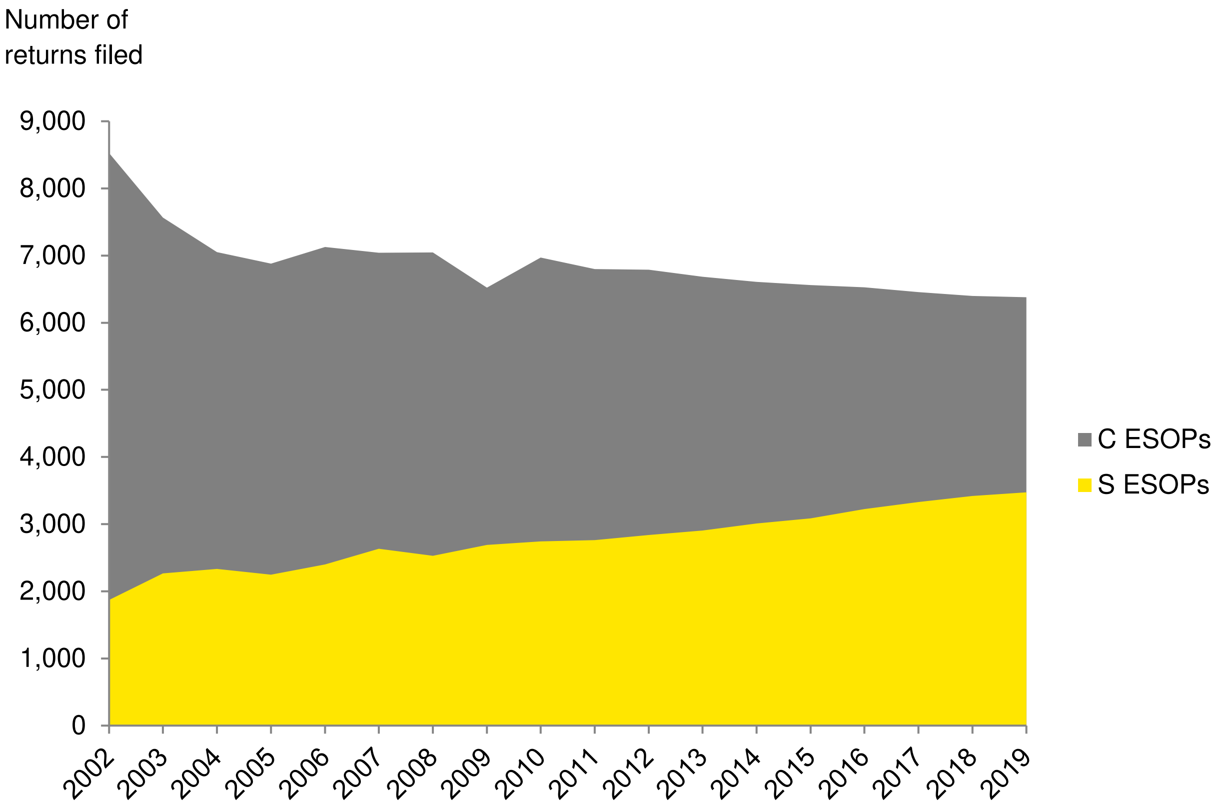
Note: Participants may or may not be the same individuals across plans. Participant figures for S ESOPs and other defined contribution plans include participants with account balances while the participant figure for defined benefit plans includes active participants, retired and separated participants receiving or entitled to receive future benefits, and beneficiaries of deceased participants receiving or entitled to receive future benefits.
Source: US Department of Labor, Form 5500 data; EY analysis.

It is important to note that even considering the full range of retirement plans offered by S ESOP companies does not capture the full set of retirement options available to their employees. In addition to the employer-based retirement plans provided by S ESOP companies, employees also have access to Social Security and Individual Retirement Accounts (IRAs). Furthermore, employees who move between places of employment may have assets in an additional employer-based retirement plan. S ESOPs represent a significant addition to the general set of retirement options available to American workers.

C. S ESOP as a share of total ESOPs

From 2002 through 2019 S ESOPs accounted for an increasing share of all ESOPs. The number of S ESOPs expanded during this time, while total ESOPs (S corporation and C corporation) declined. In other words, as the number of retirement plans designed to provide opportunities for employee ownership fell overall, the number of S ESOPs increased. In 2002, S ESOPs were 22% of ESOP plans, but by 2012 they accounted for 42% of all ESOPs and by 2019 they accounted for 54% of all ESOPs. For purposes of comparison with data on all ESOPs from the Private Pension Plan Bulletin Abstracts, S ESOPs with only one active, retired, or separated participant were excluded. This adjustment affects a negligible number of filings in recent years due to a statutory change that generally applies to S Corporation ESOPs effective for plan years beginning after December 31, 2004.

Figure 7. Trends in ESOPs, 2002-2019 (other than plans covering 1 participant)



Note: ESOP summary statistics exclude plans covering one participant, defined as the active, retired, and separated participants. For comparison purposes, those plans were excluded from the S ESOP total. S ESOP filings that listed no net assets, distributions, or participants with account balances were also removed.

Source: EY analysis using Form 5500 and Private Pension Plan Bulletin Abstracts, 2002-2019.

V. S ESOP employee-owner benefits

Economic research finds that the S ESOP structure and the employee ownership model it supports helps align the incentives between workers and employers. This incentive alignment has been found to improve job quality, productivity, and resilience during recessions.[8] One study quantified the benefits to a typical worker from S ESOP employment that accrue from: 1) firm contributions associated with their ownership stake, 2) the gains from job security, and 3) accruals of equity within a S ESOP.[9] This report followed a similar approach to estimate an annual benefit of nearly $26,000 to a typical employee-owner.

A. Firm contributions to employee-owners

One benefit that accrues to S ESOP employee-owners is the firm contribution to their retirement accounts. This report calculates firm contribution amounts by S ESOPs to their employee-owners in 2019. These firm contributions can only be earned by working for an S ESOP and being an employee-owner.[10] As displayed in Table 7, total firm contributions from S ESOPs in 2019 were approximately $3.0 billion. When averaged over the total number of participants with account balances, the per participant contribution was about $3,200 on average.

Table 7. Annual S ESOP employee-owner benefits, 2019
nominal dollars

	Average individual gains	Aggregate gains
S ESOP firm contributions[1]	$3,150	$3.0 billion
Savings attributable to job security[2]	$4,100	$3.9 billion
Direct employee-owner benefits	***$7,260***	***$6.9 billion***
Accruals of equity within a S ESOP[3]	$18,620	$17.7 billion
Indirect employee-owner benefits	***$18,620***	***$17.7 billion***
Total employee-owner benefits	**$25,900**	**$24.6 billion**

[1] Calculated as the total employer contributions in 2019 divided by participants with account balances.
[2] The estimate is calculated by comparing a full-time worker who earns the median weekly earnings for a full year in 2019 to a laid off worker who spends the median weeks unemployed searching for a new job and earns 10% less when taking a new job for the remaining weeks in the year. The estimate assumes unemployment insurance compensation replaces half the lost wages during the nine weeks without a job. The analysis assumes S-ESOP employees have 50% fewer job losses and attribute that to gains to the individual and aggregate. Median weekly earnings and median weeks unemployed are from the Bureau of Labor Statistics data.
[3] The equity stake amount ($153,900) is the average net asset amount per participant from the Form 5500 analysis and the return (12.1%) from the same analysis.
Source: EY analysis using Department of Labor and Bureau of Labor Statistics data.

B. Savings attributable to job security

Another benefit that accrues to S ESOP employee-owners is job security. This report captures this benefit by estimating the wages that would have been lost from a typical unemployment spell and the degradation in wages the generally occurs after such spells. To estimate the annual benefits from increased job security, this report assumes a hypothetical employee in 2019 earns the median weekly earnings as reported by the Bureau of Labor Statistics (BLS) for an entire year.[11] This is the baseline for comparison to a hypothetical worker with an unemployment spell.

The report assumes a laid off worker will spend nine weeks unemployed, the median weeks of unemployment in 2019.[12] Research indicates that unemployment compensation generally replaces half of lost wages.[13] After the unemployment spell, it is assumed that the worker finds a new job, which research indicates would generally pay, on average, 10% less than median weekly earnings.[14] This represents the lost wages from being laid off at a job.

If S ESOPs prevented all job loss, all of the lost wages would be attributed as benefits. Survey and economic research indicate that ESOP companies retain employees at higher rates during recessions relative to non-ESOP firms, especially during recessions.[15] Given the reported benefits of job retention from such surveys and the difficulty of measuring layoffs during periods of economic expansion, this report assumes that S ESOPs lay off employees at half the rate of firms generally (i.e., the risk to losing a job is half as much).

The average annual employee benefit from S ESOP job security is estimated to be $4,110. This benefit is $3.9 billion when aggregated across all S ESOPs participants with account balances.

C. Accruals of equity within a S ESOP

S ESOP employee owners have an equity stake in the S ESOP company, and the growth in that ownership stake represents a benefit to the employee-owner. This report uses the average accrual in the equity stake to represent the growth in the value of employee ownership in the business. It is listed as an indirect benefit because it represents the annual return to savings accruing in S-ESOP employee owners' savings. These gains could be withdrawn in the future as an employee-owner retires or otherwise separates from the S ESOP.

This report uses the average account balance from the panel sample used to calculate the total return to calculate the equity stake. The per participant balance is approximately $153,900, which earns an annual return of 12.1% from 2002 through 2019. This implies an average annual accrual in the equity stake of $18,620 (i.e., 12.1% of $153,900). When aggregated across all S ESOP participants with account balances, it provides an approximate benefit of $17.7 billion.

VI. Caveats and limitations

Any modeling effort is only an approximate depiction of the economic forces it seeks to represent, and this analysis is no exception. Although various limitations and caveats might be listed, several are particularly noteworthy:

- **Estimates are limited by available public information.** The analysis relies on information reported by government agencies (primarily the Department of Labor). The analysis did not attempt to verify or validate the information.

- **Estimates are limited by information available.** The Department of Labor's Form 5500 data is continuously updated as filings occur. Additionally, plans will amend previous years' data as needed. This could alter the aggregate and average numbers estimated in this report. The report did not attempt to adjust or compare how updating previous filings would or have affected the data.

- **Past trends may not be indicative of future outcomes.** As with any analysis of investment returns, past trends do not guarantee future outcomes. Future returns could vary significantly from previous trends. This applies to returns from S ESOPs and to any other market index or investment.

- **The panel estimates could include survivorship bias.** The total return analysis includes companies that have lasted from 2002 through 2019. Although the report does not perform further analysis of business practices, it would be safe to assume stronger and better performing companies are more likely to last through almost two decades. A similar limitation applies to S&P 500 index except when poor performing companies drop of the index, they are replaced by more valuable companies.

- **Estimates of job stability likely vary based on the overall economy.** Job stability estimates apply to economy at full employment. The majority of the years analyzed in this report occurred during an expanding economy. As noted above previous research indicates ESOPs could retain employees at a higher rate than other firms during recessions.

- **Estimates of equity stake will vary based on individual.** The estimate of average accrual in equity stake uses the per participant net assets from the panel of companies. Individual accounts and companies will vary depending upon personal financial decisions, business practices, and profitability.

- **Estimates could be affected by future legislative changes.** New laws passed by Congress could affect S ESOP returns. This analysis did not adjust for legislative changes made during the years analyzed.

- **Estimates do not reflect the impacts of COVID-19.** The analysis only includes Form 5500 filings through 2019. The COVID-19 pandemic and recession likely affected S ESOPs in ways that are not captured in this report.

Appendix. Data and methodology

Plan-year definition

The raw Form 5500 datasets used in the analysis are primarily categorized by plan-year start date. The Private Pension Plan Bulletin Abstracts are categorized by plan-year end date. The majority of S ESOP plans are on calendar years, meaning that the plan-year start and end dates fall within the same calendar year.

To check for the potential impact of the plan-year definition discrepancy, a year lag was used for both total distributions from 2002 through 2019 and distributions per participant. When years 2002 through 2019 from the Form 5500 data for S ESOPs were compared with years 2003 to 2019 for 401(k) data, the conclusions do not change. S ESOP distributions increased 1,350% from 2002 to 2018 and 401(k) distributions increased 267% from 2003 to 2019. The unadjusted increases were 1,350% for S ESOPs and 253% for 401(k)s. On a distributions per participant basis, the lagged estimates result in S ESOP distributions per participant in that are 21% higher than 401(k) distributions. The unadjusted difference was 25%.

Using a full year lag is the largest possible adjustment and assumes that none of the records from Form 5500 have plan-year start and end dates in the same calendar year, while in reality the majority do. The true impact of the plan-year definition discrepancy is, therefore, smaller than the figures presented above.

Definition of distributions

Section II above includes the definition of distributions for S ESOPs from both Schedule H and Schedule I. The Private Pension Plan Bulletin Abstracts use a somewhat different definition than either Schedule H or Schedule I. While Schedule H shows a breakdown between distributions directly to participants and payments to insurance carriers and other organizations providing benefits and Schedule I simply shows total benefits paid, the Abstracts show benefits paid directly to participants and premium payments to insurance carriers.[16] This definition includes some of the benefits the analysis excludes from Schedule H, but excludes some of the benefits included on Schedule I. However, due to the small size of these components of benefits for S ESOPs (as noted above, they accounted for 0.5% or less of distributions directly to participants in every year), this discrepancy was assumed to be immaterial.

Definition of participants

The Private Pension Plan Bulletin Abstracts report counts of active and total participants. The total participants count includes all active, retired, and separated participants, including those who have not made or received a contribution to the plan. For plans that filed using the Form 5500 Short Form, the count may include deceased participants whose beneficiaries are receiving or entitled to receive future benefits. It also includes double counting of individuals who are on more than one plan.[17]

The definition of S ESOP participants used in the distribution per participant comparison was adjusted to match the methodology of the Abstracts. It excludes deceased participants and does not attempt to adjust for potential double-counting. As noted above, this analysis found that companies offering an ESOP are substantially more likely to offer a second direct contribution plan, suggesting that double counting may pose a more significant issue for ESOPs than for 401(k)s.

Data considerations

The data had an outlier that significantly increased the total net assets of the S ESOP sample 2018 and 2019. Further inquiry into the outlier determined that it has been an S ESOP for many years but could not determine why it was not included in the dataset. Additionally, given the nature of its many businesses, there could be aspects of the business that may increase its S ESOP net assets but not be part of the S corporation. Given these considerations, the firm was omitted from the sample. If included in the analysis, the net assets and net assets per participant would be approximately 15-16% higher in 2018 and 2019. The growth rate in those two years with this S ESOP included was comparable to the growth rate without the company in the sample.

Endnotes

[1] For more details see, “Contributions of S ESOPs to participants’ retirement security”, EY, March 2015, https://esca.us/wp-content/uploads/2021/10/EY-ESCA-S-ESOP-retirement-security-analysis-2015.pdf

[2] The primary difference between net assets and account balances is in the case of leveraged S ESOPs. A leveraged S ESOP uses loans to purchase company shares, which are not immediately allocated to participants. Instead, they are held by the ESOP trust and are allocated to participants’ ESOP accounts as the loan is repaid. When the value of newly acquired assets equal the liability incurred to acquire them, there is no difference between net assets and assets allocated to participants. Potential differences arise as the values of unallocated shares change before the loan has been repaid. The analysis assumes that, in aggregate, plan liabilities offset unallocated plan assets.

[3] The estimated number of employees is calculated using data on active participants by plan and the relationship between active participants and total employees from a prior ESCA study that found that the correlation coefficient between active participants in S ESOPs and employment is 0.9 and that employment in S ESOPs is, on average, 40% higher than the number of active participants. Alex Brill, “An Analysis of the Benefits S ESOPs Provide the US Economy and Workforce,” A report prepared on behalf of the Employee-Owned S Corporations of America, July 2012, https://esca.us/wp-content/uploads/2021/07/Brill_S_ESOP_Study_2012.pdf

[4] US Department of Labor Bureau of Labor Statistics, “Establishments offering retirement and health care benefits,” National Compensation Survey, Table 1, 2019.
https://www.bls.gov/ncs/ebs/benefits/2019/ownership/private/table01a.pdf

[5] Ibid

[6] For more details see Table E19, Employee Benefits Security Administration, “Private Pension Plan Bulletin Historical Tables and Graphs 1975-2019,” US Department of Labor, September 2021, https://www.dol.gov/sites/dolgov/files/ebsa/researchers/statistics/retirement-bulletins/private-pension-plan-bulletin-historical-tables-and-graphs.pdf

[7] At the time the analysis accessed the data, the 2019 data seemed incongruent with previous trends. Given the data is continuously updated as filings and amendments occur, the analysis used 2018 data which should be more complete and be less subject to future amendments and changes.

[8] For more details on the potential benefits and costs see, Douglas Kruse, “Does employee ownership improve performance? Employee ownership generally increases firm performance and worker outcomes”, IZA World of Labor, December 2016, https://wol.iza.org/uploads/articles/311/pdfs/does-employee-ownership-improve-performance.pdf

[9] See Steve Freeman and Michael Knoll, “S Corp ESOP Legislation Benefits and Costs: Public Policy and Tax Analysis,” University of Pennsylvania Center for Organizational Dynamics, Working Paper #08-07, July 29, 2008.

[10] A similar benefit could exist for an ESOP that does not file as a S corporation. The contribution estimate does not apply to other forms.

[11] The analysis uses the median usual weekly earnings of full-time wage and salary workers from the Bureau of Labor Statistics for the fourth quarter of 2019 ($934).

[12] Median weeks of unemployment from the Bureau of Labor Statistics Household Survey. If the average weeks of unemployment were used, the duration of the unemployment spell would be longer.

[13] For more details see, Peter Ganong, Pascal Noel, and Joseph Vavra, “US Unemployment Insurance Replacement Rates During the Pandemic,” NBER Working Paper 27216, May 2020. https://www.nber.org/digest/jul20/unemployment-benefit-replacement-rates-during-pandemic. According to the paper, Nevada is close to the median with a replacement rate of 52%. The report assumes 50% replacement rate and does not make any adjustment for benefit caps or other benefits that may be affected by unemployment compensation.

[14] Displaced workers earn approximately 10% lower on average for decades after the job loss. For more details see, William Carrington and Bruce Fallick, “Why Do Earnings Fall with Job Displacement?”, Federal Reserve Bank of Cleveland, Working Paper 14-05, June 17, 2014, https://www.clevelandfed.org/en/newsroom-and-events/publications/working-papers/2014-working-papers/wp-1405-why-do-earnings-fall-with-job-displacement.aspx

[15] For more details see, Employee Ownership Foundation, Rutgers School of Management and Labor Relations, "Employee-Owned Firms in the Covid-19 Pandemic: How Majority-Owned ESOP & Other Companies Have Responded to the Covid-19 Health and Economic Crises", accessed December 10, 2021, https://employeeownershipfoundation.org/sites/eof-master/files/2020-10/EOF_COVID_2020.pdf and Fidan Ana Kurtulus and Douglas L. Kruse, "How Did Employee Ownership Firms Weather the Last Two Recessions? Employee Ownership, Employment Stability, and Firm Survival: 1999–2011", W.E. Upjohn Institute for Employment Research, 2017, https://research.upjohn.org/cgi/viewcontent.cgi?article=1259&context=up_press#

[16] For more details see, Employee Benefits Security Administration, "Private Pension Plan Bulletin Historical Tables and Graphs 1975-2019," US Department of Labor, September 2021, https://www.dol.gov/sites/dolgov/files/ebsa/researchers/statistics/retirement-bulletins/private-pension-plan-bulletin-historical-tables-and-graphs.pdf

[17] Ibid.